

Report
of the
Examination of
Middlesex Insurance Company
Stevens Point, Wisconsin
As of December 31, 2003

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State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

Jim Doyle, Governor
Jorge Gomez, Commissioner

Wisconsin.gov

June 6, 2005

125 South Webster Street • P.O. Box 7873
Madison, Wisconsin 53707-7873
Phone: (608) 266-3585 • Fax: (608) 266-9935
E-Mail: information@oci.state.wi.us
Web Address: oci.wi.gov

Honorable Jorge Gomez
Secretary, Midwestern Zone, NAIC

Commissioner of Insurance
State of Wisconsin
125 South Webster Street
Madison, Wisconsin 53702

Honorable Alfred W. Gross
Chair, Financial Condition (E) Committee,
NAIC

Commissioner of Insurance
Commonwealth of Virginia
1300 East Main Street
Richmond, Virginia 23219

Honorable Julianne M. Bowler
Secretary, Northeastern Zone, NAIC
Commissioner of Insurance
Commonwealth of Massachusetts
One South Station, 5th Floor
Boston, Massachusetts 02110-2208

Honorable John Morrison
Secretary, Western Zone, NAIC
Commissioner of Insurance
State of Montana
840 Helena Avenue
Helena, Montana 59601

Commissioners:

In accordance with the instructions of the Wisconsin Commissioner of Insurance, a
compliance examination has been made of the affairs and financial condition of:

MIDDLESEX INSURANCE COMPANY
Stevens Point, Wisconsin

and this report is respectfully submitted.

I. INTRODUCTION

The previous examination of Middlesex Insurance Company (Middlesex or the company) was conducted in 2000 as of December 31, 1999. The current examination covered the intervening period ending December 31, 2003, and included a review of such 2004 transactions as deemed necessary to complete the examination.

The examination consisted of a review of all major phases of the company's operations, and included the following areas:

- History
- Management and Control
- Corporate Records
- Conflict of Interest
- Fidelity Bonds and Other Insurance
- Employees' Welfare and Pension Plans
- Territory and Plan of Operations
- Affiliated Companies
- Growth of Company
- Reinsurance
- Financial Statements
- Accounts and Records
- Data Processing

Emphasis was placed on the audit of those areas of the company's operations accorded a high priority by the examiner-in-charge when planning the examination.

The section of this report titled "Summary of Examination Results" contains comments and elaboration on those areas where adverse findings were noted or where unusual situations existed. Comment on the remaining areas of the company's operations is contained in the examination work papers.

The company is annually audited by an independent public accounting firm as prescribed by s. Ins 50.05, Wis. Adm. Code. An integral part of this compliance examination was the review of the independent accountant's work papers. Based on the results of the review of these work papers, alternative or additional examination steps deemed necessary for the completion of this examination were performed. The examination work papers contain documentation with respect to the alternative or additional examination steps performed during the course of the examination.

Independent Actuary's Review

An independent actuarial firm was engaged under a contract with the Office of the Commissioner of Insurance. The actuary reviewed the adequacy of the company's loss and loss adjustment expense reserves. The actuary's results were reported to the examiner-in-charge. As deemed appropriate, reference is made in this report to the actuary's conclusion.

II. HISTORY AND PLAN OF OPERATION

Middlesex was chartered in Massachusetts as the Middlesex Mutual Fire Insurance Company on March 3, 1826, and the company commenced business on March 29, 1826. The company has been the surviving entity in several mergers during its history. The company absorbed the South Danvers Mutual Fire Insurance Company in December 1928 and the Citizens Mutual Fire Insurance Company in June 1944.

In 1963 the name was changed to Middlesex Mutual Insurance Company. On October 20, 1967, Middlesex and Lynn Mutual Insurance Company (Lynn Mutual) voted to form the North Bridge Corporation, a downstream holding company. Middlesex held 80% ownership in the corporation, with the remaining 20% held by Lynn Mutual. In 1968, Middlesex and Lynn Mutual contributed their respective ownership interests in the newly established Patriot General Insurance Company, a stock property and casualty insurer, to this holding company.

Lynn Mutual was absorbed by Middlesex through a merger transaction effective December 31, 1970, thereby making Middlesex the sole owner of North Bridge and its subsidiary interests.

Middlesex entered into an agreement, dated June 6, 1974, with Sentry Insurance a Mutual Company (SIAMCO), whereby Middlesex would demutualize and be acquired by The Sentry Corporation, then a wholly owned subsidiary of SIAMCO. In June 1974, special legislation passed by the Massachusetts Legislature permitted the conversion, articles of amendment were filed with the Secretary of the Commonwealth of Massachusetts in order to execute the conversion and rename the company to its current name, and the Massachusetts Insurance Division approved the transactions. The Sentry Corporation acquired all 200,000 shares issued by the company.

In 1986, ownership of Middlesex was transferred from The Sentry Corporation to SIAMCO, its current parent, as part of an effort to separate insurance operations from non-insurance operations. On April 28, 1994, Middlesex, together with its subsidiary, Patriot General, redomiciled from Massachusetts to Wisconsin.

In 2003, the company wrote direct premium in the following states:

Wisconsin	\$18,963,644	26.6%
Massachusetts	16,220,324	22.8
California	8,557,997	12.0
Texas	7,292,089	10.2
Connecticut	7,250,912	10.2
All others	<u>12,930,712</u>	<u>18.2</u>
Total	<u>\$71,215,678</u>	<u>100.0%</u>

The company is licensed in 37 states and the District of Columbia.

The major products marketed by the company include worker's compensation and private passenger auto. Middlesex has sales representatives of all categories throughout its business territory. The company uses standard contract forms and commission schedules for its sales representatives. Independent agents and Massachusetts exclusive representative producers earn commissions, which depend on the line of business sold and application source (paper or electronic). Independent agents may also earn contingent commissions based on production volume and profitability of the business written. Direct writers, who are employees of SIAMCO, receive subsidies at the beginning of their employment, a comprehensive benefit package, are eligible for special bonuses and incentives, as well as receiving commissions generally paid to independent agents.

In the state of Wisconsin, the company is licensed to transact the following lines of business as defined by s. Ins 6.75 (2), Wis. Adm. Code:

- (a) Fire, Inland Marine, and Other Property
- (b) Ocean Marine
- (c) Disability
- (d) Liability and Incidental Medical Expense
- (e) Automobile and Aircraft
- (f) Fidelity
- (g) Surety
- (k) Worker's Compensation
- (n) Miscellaneous

The following table is a summary of the net insurance premiums written by the company in 2003. The growth of the company is discussed in the "Financial Data" section of this report.

Line of Business	Direct Premium	Reinsurance Assumed	Reinsurance Ceded	Net Premium
Fire	\$ 1,200,696	\$ 4,604,072	\$1,866,915	\$ 3,937,853
Allied lines	1,451,757	4,175,532	2,338,771	3,288,518
Homeowner's multiple peril	1,634,693	3,790,857	1,634,693	3,790,857
Commercial multiple peril	1,758,459	2,601,699	2,667,341	1,692,817
Ocean marine		8,228		8,228
Inland marine	294,464	6,461,006	442,418	6,313,052
Earthquake	3,982	101,469	6,054	99,397
Group accident and health		1,524,373		1,524,373
Other accident and health		4,887		4,887
Worker's compensation	38,733,269	48,767,110	50,147,099	37,353,280
Other liability - occurrence	1,037,577	9,806,643	1,645,252	9,198,968
Other liability - claims made		354,658		354,658
Products liability - occurrence	734,925	3,262,918	1,319,428	2,678,415
Private passenger auto liability	13,988,279	58,983,621	26,893,278	46,078,622
Commercial auto liability	2,127,901	24,209,181	3,361,121	22,975,961
Auto physical damage	8,211,977	33,608,393	13,509,713	28,310,657
Aircraft (all perils)		(3,176)		(3,176)
Fidelity	28,612	492,697	57,646	463,663
Surety	60	95,950	60	95,950
Burglary and theft	9,027	172,286	15,261	166,052
International		806	(74)	880
Reinsurance - non-proportional assumed property		(20,861)		(20,861)
Write-ins for other lines of business:				
Extended warranty		983,626		983,626
Total All Lines	<u>\$71,215,678</u>	<u>\$203,985,975</u>	<u>\$105,904,976</u>	<u>\$169,296,677</u>

Of the total net premiums written, private passenger auto liability represents 27% of the business. Auto physical damage, worker's compensation, and inland marine represent 17%, 22%, and 4%, respectively.

In addition to its direct business, the company assumes 100% of the premiums written by its subsidiary, Patriot General Insurance Company, which was \$33,827,122 in 2003. All direct and assumed business, net of cessions to nonaffiliated reinsurers, is pooled with affiliates,

SIAMCO, Dairyland Insurance Company, and Sentry Select Insurance Company. These treaties are described in the section of this examination report titled "Reinsurance."

III. MANAGEMENT AND CONTROL

Board of Directors

The board of directors consists of five members elected annually by the shareholder. Officers are elected at the board's annual meeting. Members of the company's board of directors may also be members of other boards of directors in the holding company group. The board members receive no compensation specific to their service on the board because all are employees of the parent, Sentry Insurance a Mutual Company.

The board of directors for Middlesex meets once per year. Other actions of the board are evidenced by consent resolutions signed by all directors. This practice is permitted by s. 180.0821, Wis. Stat.

Currently the board of directors consists of the following persons:

Name and Residence	Principal Occupation	Term Expires
Dale R. Schuh Stevens Point, Wisconsin	Chairman of the Board, Chief Executive Officer and President, Sentry Insurance a Mutual Company	2005
Janet L. Fagan Stevens Point, Wisconsin	Vice President and Chief Actuary, Sentry Insurance a Mutual Company	2005
William J. Lohr Stevens Point, Wisconsin	Vice President and Treasurer, Sentry Insurance a Mutual Company	2005
William M. O'Reilly Stevens Point, Wisconsin	Vice President, General Counsel and Corporate Secretary, Sentry Insurance a Mutual Company	2005
James J. Weishan Stevens Point, Wisconsin	Vice President – Investments, Sentry Insurance a Mutual Company	2005

Officers of the Company

The officers serving at the time of this examination are as follows. The officers are employed and compensated by Sentry Insurance a Mutual Company. The officers of Middlesex may also be officers of other companies in the Sentry Group. The salaries listed below are the portion of the officer's total salary that is allocated to Middlesex.

Name	Office	2004 Compensation
Dale Robert Schuh	Chief Executive Officer	\$95,749
James Craig Clawson	President	10,313
William James Lohr	Treasurer	16,896
William Michael O'Reilly	Secretary	15,383
Janet Leitner Fagan	Vice President	23,427

Committees of the Board

The company's bylaws allow for the formation of certain committees by the board of directors. The company did not have any committees at the time of the examination.

IV. AFFILIATED COMPANIES

Middlesex Insurance Company is a member of a holding company system (Sentry Insurance Group) controlled by Sentry Insurance a Mutual Company, a Wisconsin-domiciled mutual insurer. Including Middlesex, SIAMCO has 22 subsidiaries and affiliates, including 11 insurers and 11 noninsurance entities. SIAMCO is also affiliated with Dairyland County Mutual Insurance Company of Texas through common management. A chart of all of the entities in the holding company system is presented later in this section of the examination report.

A discussion of all the Sentry Insurance Group affiliated companies is included in the examination report for SIAMCO. This report includes only those affiliates with which Middlesex has reinsurance or other important affiliated relationships.

Sentry Insurance a Mutual Company

SIAMCO owns all of the issued and outstanding common stock of Middlesex. SIAMCO is licensed in all 50 states, the District of Columbia, Puerto Rico, and Canada. On a direct basis, the parent company writes a wide range of property and casualty insurance products, predominantly worker's compensation and automobile coverages. SIAMCO has a 60% participation in the affiliated pooling agreement, whereby all property and casualty business written by the Sentry Insurance Group is combined and reapportioned. The 2003 annual statement reported assets of \$4,282,734,663, liabilities of \$2,105,670,251, policyholders' surplus of \$2,177,064,411, and net income of \$116,879,367. SIAMCO was examined concurrently with Middlesex as of December 31, 2003, and the results of that examination are expressed in a separate report.

Dairyland Insurance Company

Dairyland Insurance Company is a Wisconsin-domiciled stock property and casualty insurer licensed in 44 states. The company was formed on August 1, 1965, to become successor to the Dairyland Mutual Insurance Company organized on January 8, 1953. During 1966, SIAMCO acquired all outstanding common shares, and has since held 100% ownership, though control has, at times, been indirect. At present, SIAMCO holds 100% of all outstanding common stock directly.

On its direct business, the company specializes in nonstandard auto, with some motorcycle business as well. The company also assumes 100% of the business of Dairyland County Mutual Insurance Company of Texas, a Texas county mutual. Dairyland has a 20% participation in the affiliated pooling agreement, whereby all property and casualty business written by the Sentry Insurance Group is combined and reapportioned. The 2003 annual statement reported assets of \$973,840,753, liabilities of \$676,989,323, policyholders' surplus of \$296,851,430, and net income of \$25,494,952. Dairyland was examined concurrently with Middlesex as of December 31, 2003, and the results of that examination are expressed in a separate report.

Sentry Select Insurance Company

Sentry Select Insurance Company is a property and casualty insurer incorporated on August 1, 1929, as the Fulton Fire Insurance Company under the laws of New York. On May 8, 1969, Deere & Company acquired the company from Hanover Insurance Company of New York and changed its name to John Deere Insurance Company. The company redomiciled to the State of Illinois on December 31, 1982. SIAMCO acquired 100% indirect ownership in connection with the acquisition of Sentry Insurance Holding Company on September 30, 1999, and the name was changed to Sentry Select Insurance Company. On January 1, 2001, the company redomiciled to the state of Wisconsin.

Sentry Select is licensed in all 50 states and the District of Columbia. Of its direct business, the company writes 51% in auto, 10% in inland marine and 14% in worker's compensation lines of business. Sentry Select also assumes 100% of the business from Sentry Casualty Company. Sentry Select has a 10% participation in the affiliated pooling agreement. The 2003 annual statement reported assets of \$532,976,838, liabilities of \$385,419,139, policyholders' surplus of \$147,557,700, and net income of \$11,599,064. Sentry Select was examined concurrently with Middlesex as of December 31, 2003, and the results of that examination are expressed in a separate report

Patriot General Insurance Company

Patriot General Insurance Company is a property and casualty insurer incorporated under its present name pursuant to the laws of the Commonwealth of Massachusetts on January 2, 1968. SIAMCO acquired 100% indirect ownership of Patriot General in June 1974 in connection with the acquisition of Middlesex. On April 28, 1994, Patriot General redomiciled to the state of Wisconsin.

Patriot General is licensed in 21 states, with approximately 71% of all of its premiums written in Florida and Georgia. The company writes predominantly auto and worker's compensation lines of business. The company cedes 100% of its business to Middlesex Insurance Company, its immediate parent. The 2003 annual statement reported assets of \$19,241,651, liabilities of \$1,206,239, policyholders' surplus of \$18,035,424, and net income of \$627,101. Patriot General was examined concurrently with Middlesex as of December 31, 2003, and the results of that examination are expressed in a separate report.

Sentry Investment Management, Inc.

Sentry Investment Management, Inc., a Delaware corporation organized on June 13, 1969, manages the investment portfolios of SIAMCO and its affiliates, subject to the direction of their respective boards of directors. As of December 31, 2003, the corporation reported \$354,027 in assets, \$218,537 in liabilities, \$135,490 in stockholder's equity, and \$5,538 in net income. The company is a wholly owned subsidiary of SIAMCO.

Affiliated Agreements

Middlesex has no employees of its own. All operations are conducted by employees of its parent organization, SIAMCO, in accordance with its business practices and internal controls. In addition, the company's operations are affected by written agreements with Sentry Insurance Group affiliates. The reinsurance contracts are described in the "Reinsurance" section of this report. A brief summary of the other agreements follows.

Service Agreement

Middlesex entered into an intercompany servicing agreement with SIAMCO effective December 31, 2003. This agreement was amended and restated as of March 19, 2004, to

include an updated version of Exhibit 1, Intercompany Settlement Policy described below, to add Parker Centennial Assurance Company (Parker Centennial). Services provided by SIAMCO include, but are not limited to, premium accounting and collection, budgeting, disbursement services, administration of loss and loss adjustment expense payments, and management services. The agreement permits Middlesex to audit records pertaining to services performed by SIAMCO under this agreement. Termination, or changes in the terms and conditions of service, may be effected by either party on 30 days' written notice. The form of the agreement is structured so that essential aspects of the allocation methodology itself are referenced in attachments which are periodically updated.

Intercompany Settlement Policy

The Intercompany Settlement Policy has been amended and restated to add or delete companies as necessary. This contract was last amended and restated as of March 19, 2004, to add Parker Centennial. The cash management area settles intercompany balances, in SLAP where possible, based on policies and procedures listed in the agreement for daily, weekly, monthly, semi-annual and annual settlements. Other settlements under the agreement include reinsurance balances, which are to be settled according to the terms contained in the reinsurance agreements, and Sentry Aviation Services and Sentry Services, which are settled as funds are available.

Sentry Complex Income Tax Allocation Agreement

On February 22, 1983, the SIAMCO board of directors adopted a written federal income tax allocation policy for all companies that are party to SIAMCO's consolidated return. This agreement has been amended and restated to add or delete companies as needed. The latest amended and restated agreement is effective December 31, 2003, and was amended on March 19, 2004, to add Parker Centennial. The key premise of this policy is that parties to the consolidated return that receive a tax reduction through utilization of some other member's tax loss are to compensate that member for the use of the loss. Federal income tax payable and tax benefits receivable are to be settled among the participants on the consolidated return on the same dates as would be required of each participant on a separate return basis.

Joint Investment Agreement

Effective January 1, 1980, the company entered into a joint investment agreement with various other affiliates to establish the Sentry Liquid Asset Partnership (SLAP), a joint venture organized pursuant to the Wisconsin Uniform Partnership Act. This agreement has been amended and restated to add or delete companies as needed. The fifth amended and restated agreement was entered into as of September 1, 2004, to delete Sentry Life Insurance Company of New York (SLONY). SIAMCO is designated as the managing partner, though the agreement permits a change by a majority decision of the participants. A participant may withdraw from the joint venture upon the delivery of written notice to the managing partner. The joint venture shall dissolve at such time as only one participant remains in the joint venture.

The business of the joint venture consists of investing and reinvesting funds contributed by the members in short-term obligations of banks, corporations, and the U. S. federal government with a maximum duration of twelve months. It functions in a manner analogous to a short-term bond mutual fund. Investment advisory services are provided by Sentry Investment Management, Inc. This office has directed all Wisconsin-domiciled Sentry companies to report their respective balances in SLAP as a one-line entry on Schedule DA – Part 1 (Short-Term Investments).

Agreement with Sentry Investment Management, Inc.

On April 23, 1991, the company entered into an investment advisory agreement with Sentry Investment Management, Inc. (SIMI). This contract was amended and restated as of December 31, 2003. Under this contract, SIMI is employed to manage and direct the investment and reinvestment of the assets of Middlesex, subject to the control of its board of directors. SIMI agrees to comply with the company's articles, bylaws, investment policies, and all applicable federal or state laws. Provided it acts in good faith, the advisor is held harmless except in the event of a loss resulting from willful misfeasance, bad faith, gross negligence, or reckless disregard. SIMI charges the company a monthly fee computed as follows:

One twelfth (1/12) of an amount equal to the sum of (a) and (b)

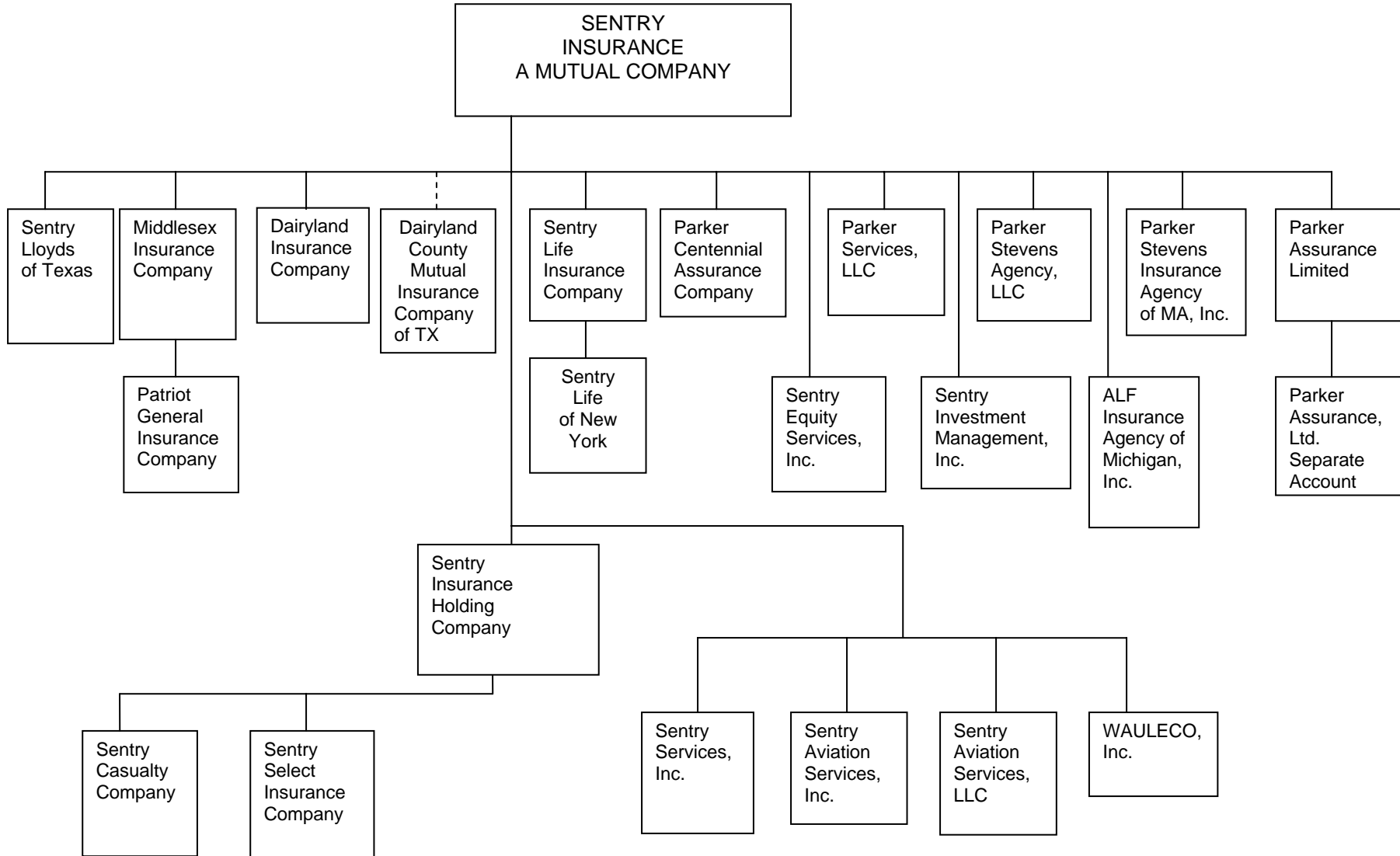
- (a) Common stocks, excluding those of affiliates:
.379 percent (\$3.79 per \$1,000) of market value;
- (b) Bonds and preferred stocks, excluding those of affiliates:
.0379 percent (\$.379 per \$1,000) of market value.

In addition, the actual cost of any expense borne by the advisor on behalf of the company is reimbursed. The contract may be terminated by either of the parties with 60 days' written notice.

General Expense Allocation Agreement

In 1993, the insurance companies of the Sentry Insurance Group entered into a written general expense allocation agreement. The agreement formalized the parties' consent to an accounting allocation process that had been in place since 1982. This agreement has been amended and restated to add or delete companies as needed. The latest amended and restated agreement is effective December 31, 2003, and was amended on March 19, 2004, to add Parker Centennial. Under the agreed procedure, expenses are first grouped and assigned to cost pools, each of which is distinguished by one or more of four characteristics, including activity, location, center, and division. Expenses, once assigned to cost pools, are then allocated to specific insurance products. An expense is not assigned to a specific legal entity until after it is coded to a cost pool and then to a specific product. Allocation at each phase of this process, outlined here in simplified form, is based on specific identification, utilization estimates developed from such criteria as premium or claim volume, time studies, or other rational means of distribution.

**Sentry Group
Organizational Chart
As of December 31, 2004**



V. REINSURANCE

The company's reinsurance portfolio and strategy is described below. A list of the companies that have a significant amount of reinsurance in force at the time of the examination follows.

Affiliated Property and Casualty Pooling Agreement

The company participates in a pooling arrangement with certain of its property and casualty affiliates. Dairyland Insurance Company, Middlesex Insurance Company, and Sentry Select Insurance Company cede 100% of their direct and assumed premiums, losses, loss adjustment expenses, and underwriting expenses, net of all cessions to nonaffiliated parties, to Sentry Insurance a Mutual Company. The net pooled business is then distributed according to the participations listed below. Specifically excluded from the pooling are income and expenses related to investment operations.

Dairyland, Middlesex, and Sentry Select are direct co-parties to the automatic nonaffiliated ceding reinsurance agreements of SIAMCO along with all of SIAMCO's other property and casualty affiliates, including Dairyland County Mutual Insurance Company of Texas, Patriot General Insurance Company, Sentry Lloyds of Texas, and Sentry Casualty Company. SIAMCO administers all aspects of the pooled business, including placement of reinsurance with nonaffiliates. However, reinsurance with nonaffiliated parties is transacted in the names of SIAMCO, Dairyland, Middlesex, and Sentry Select each for its own direct and assumed business, prior to pooling. After nonaffiliated cessions are made, the net business of each participant is pooled, and all of the net retained business of SIAMCO, Dairyland, Sentry Select and Middlesex is derived from the pool. Additional terms of the pool are outlined below:

Effective date:	December 31, 2003 (Amended and Restated)	
Participation:	Sentry Insurance a Mutual Company	60%
	Dairyland Insurance Company	20%
	Middlesex Insurance Company	10%
	Sentry Select Insurance Company	10%
Termination:	By mutual agreement of the parties in writing, or by 90 days' advance notice by any one party to the other parties. In either event, such termination shall not be made effective at other than a subsequent calendar year-end.	

Affiliated Assuming Contracts

1. Type: 100% Quota Share Reinsurance
- Reinsured: Patriot General Insurance Company
- Scope: All business written by the reinsured
- Ceding company retention: None
- Coverage: 100% of all loss and loss adjustment expenses incurred by the reinsured
- Premium: 100% of gross premiums written and assumed by the reinsured
- Commission: An amount equal to the actual underwriting expenses, policyholders' dividends, and unallocated claim expenses of the reinsured, with return commission allowed on return premiums at the same rate
- Effective date: December 31, 2003 (Amended and Restated)
- Termination: This treaty may be terminated as of 11:59 p.m. Eastern Standard Time, on the last day of any calendar month by either party giving the other 30 days' notice by registered mail, or at any time by mutual consent of both parties; in the event of termination, the reinsurer shall return to the company the full unearned premium reserve, computed on the monthly pro rata basis of the effective date of cancellation, less the ceding commission.

In effect, Patriot General Insurance Company does not retain any net premiums written, net premiums earned, net losses incurred, loss adjustment expenses, or underwriting expenses under this contract and, therefore, cannot incur an underwriting profit or loss as long as this treaty is in force.

Nonaffiliated Ceding Contracts

1. Type: Multiple Line Excess of Loss
- Reinsurer: See Table A at the end of this section
- Scope: Property and casualty business
- Retention: \$2,500,000, each risk, each occurrence
- Coverage: The amount of ultimate net loss, including loss adjustment expenses, in excess of the company's retention of \$2,500,000 per risk. Reinsurer risk not to exceed \$12,500,000 as respects any one risk each loss, nor shall it exceed \$25,000,000 all risks involved in any one occurrence.

Premium:	Annual minimum deposit of \$21,920,000; actual premium is 1.65% of subject net premiums earned for property business and 1.65% of subject net earned premium for casualty business.
Commissions:	None
Effective date:	January 1, 2004
Termination:	Company may terminate upon 60-day notice to reinsurer. Reinsurer may terminate upon 90-day notice to company.
2. Type:	Multiple Line Clash and Contingency Excess
Reinsurers:	See Table B at the end of this section
Scope:	Property and casualty losses
Commission:	None
Effective date:	January 1, 2004
Termination:	Company may terminate upon a 10-day notice to reinsurer.
a. First Layer Retention:	\$15,000,000 each risk, each occurrence
Coverage:	Ultimate net loss in excess of the company's retention, up to a limit of \$5,000,000 per loss occurrence, and \$15,000,000 in aggregate for the contract year
Premium:	Annual minimum deposit premium of \$748,000; actual premium is .0563% of subject net earned premium
b. Second Layer Retention:	\$20,000,000 each risk, each occurrence
Coverage:	Ultimate net loss in excess of the company's retention, up to a limit of \$10,000,000 per loss occurrence, and \$20,000,000 in aggregate for the contract year
Premium:	Annual minimum deposit premium of \$692,000; or .0521% of subject direct earned premium
c. Third Layer Retention:	\$30,000,000 each risk, each occurrence
Coverage:	Ultimate net loss in excess of the company's retention, up to a limit of \$20,000,000 per occurrence, and \$40,000,000 in aggregate for the contract year
Premium:	Annual minimum deposit premium of \$920,000; or .0690% of subject direct earned premium

- d. Fourth Layer
Retention: \$50,000,000 each risk, each occurrence
- Coverage: Ultimate net loss in excess of the company's retention, up to a limit of \$20,000,000 per occurrence, and \$40,000,000 in aggregate for the contract year
- Premium: Annual minimum deposit premium of \$742,000; or .0558% of subject direct earned premium
3. Type: Property Catastrophe Excess of Loss
- Reinsurers: See Table C at the end of this section
- Scope: Property
- Effective date: January 1, 2004
- Termination: Company or reinsurer may terminate agreement upon 90-day notice to each other
- a. First Layer
Retention: \$10,000,000 each occurrence plus 5% of the next layer
- Coverage: 95% of the company's ultimate net loss, including loss adjustment expenses, in excess of the company's retention, up to a limit of \$5,000,000 per loss occurrence, and \$10,000,000 aggregate for the contract year
- Premium: Annual deposit of \$701,100; actual premium is .4100% of subject net earned premium
- b. Second Layer
Retention: \$15,000,000 each occurrence plus 5% of the next layer
- Coverage: 95% of the company's ultimate net loss, including loss adjustment expenses, in excess of the company's retention, up to a limit of \$15,000,000 per loss occurrence, and \$30,000,000 aggregate for the contract year
- Premium: Annual deposit of \$1,453,500; actual premium is .8500% of subject net earned premium
- c. Third Layer
Retention: \$30,000,000 each occurrence plus 5% of the next layer
- Coverage: 95% of the company's ultimate net loss, including loss adjustment expenses, in excess of the company's retention, up to a limit of \$45,000,000 per loss occurrence, and \$90,000,000 aggregate for the contract year
- Premium: Annual deposit of \$1,966,500; actual premium is 1.1500% of subject net earned premium

4. Type: Worker's Compensation Excess of Loss
- Scope: Worker's Compensation and Employer's Liability
- Effective date: January 1, 2004
- Termination: December 31, 2004
- Reinsurers: American Re-insurance Company – 75%
Aspen Insurance UK Limited – 25%
- Retention: \$2,500,000 each occurrence
- Coverage: The ultimate net loss in excess of company's retention, up to a limit of \$2,500,000 per loss occurrence, with unlimited reinstatements, and \$2,500,000 aggregate for terrorism for the contract year
- Premium: Annual minimum deposit of \$3,960,000 or 1.268% of subject net earned premium
5. Type: Consumer Products Residential Property Per Risk Excess of Loss
- Reinsurer: Aspen Insurance U.K. Limited
- Scope: Residential property business
- Effective Date: June 1, 2004
- Termination: June 1, 2005
- Retention: \$1,250,000 each loss, each risk
- Coverage: The ultimate net loss in excess of \$1,250,000 each and every loss, each and every risk, but not to exceed \$1,250,000 each and every loss, each and every risk, subject to an occurrence limit of liability of \$2,500,000
- Premium: Subject to an occurrence limit of liability of \$2,500,000. Annual minimum deposit of \$50,000 or .119% of subject gross net earned premium

Table A
Multiple Line Excess of Loss
Participation Schedule

Reinsurer	Participation
American Re-insurance Company	40.0%
AXIS Reinsurance Company	15.0
Converium Reinsurance (North America) Inc.	5.0
Motors Insurance Company	14.0
Hannover Ruckversicherungs-Aktiengesellschaft	14.0
Aspen Insurance UK Limited	<u>12.0</u>
Total	<u>100.0%</u>

Table B
Multiple Line Clash
Participation Schedule

Reinsurer	Participation Layers			
	1st	2nd	3rd	4th
American Re-insurance Company	8.0%	0.0%	0.0%	0.0%
AXIS Reinsurance Company	0.0	15.0	15.0	0.0
Endurance Reinsurance Corporation of America	15.0	15.0	18.0	21.0
Folksamerica Reinsurance Company	25.0	20.0	10.0	10.0
Hannover Ruckversicherungs-Aktiengesellschaft	15.0	15.0	15.0	15.0
Liberty Mutual Insurance Company	7.0	4.0	3.5	2.5
New Jersey Re-Insurance Company	0.0	6.0	6.0	6.0
Platinum Underwriters Reinsurance, Inc.	0.0	0.0	17.5	20.5
Swiss Reinsurance America Corporation	0.0	15.0	0.0	0.0
Transatlantic Reinsurance Company	0.0	0.0	5.0	5.0
XL Reinsurance America Inc.	30.0	0.0	0.0	0.0
Aspen Insurance UK Limited	<u>0.0</u>	<u>10.0</u>	<u>10.0</u>	<u>20.0</u>
Total All Participants	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>

Table C
Property Catastrophe Excess of Loss
Participation Schedule

Reinsurer	1st Layer	Participation 2nd Layer	3rd Layer
Converium Reinsurance (North America) Inc.	3.00%	4.00%	5.00%
Everest Reinsurance Company	10.00	9.00	9.00
Folksamerica Reinsurance Company	5.00	5.00	5.00
Liberty Mutual Insurance Company	4.00	3.50	2.00
New Jersey Re-Insurance Company	5.00	3.00	1.00
Shelter Mutual Insurance Company	3.50	3.50	3.00
State Automobile Mutual Insurance Company	0.00	1.00	1.00
Transatlantic Reinsurance Company	10.00	8.00	12.00
Endurance Specialty Insurance Ltd.	9.50	7.00	7.00
Hanover Re (Bermuda) Ltd.	5.00	5.00	5.00
Allied World Assurance Company Ltd.	15.00	15.00	15.00
IPCR Limited	15.00	15.00	15.00
Montpelier Reinsurance Ltd.	6.00	6.00	6.00
PXRE Reinsurance Ltd.	3.00	3.00	3.00
Sirius International Insurance Corporation	1.00	1.00	1.00
Aspen Insurance UK Limited	0.00	0.00	2.00
Odyssey America Reinsurance Corporation	0.00	3.00	0.00
Lloyd's Syndicate KLN #0510	0.00	1.00	1.00
Lloyd's Syndicate AFB #0623	0.00	0.46	0.46
Lloyd's Syndicate AFB #2623	0.00	0.54	0.54
Lloyd's Syndicate BRT #2987	<u>0.00</u>	<u>1.00</u>	<u>1.00</u>
Total All Participants	<u>95.00%</u>	<u>95.00%</u>	<u>95.00%</u>

VI. FINANCIAL DATA

The following financial statements reflect the financial condition of the company as reported to the Commissioner of Insurance in the December 31, 2003, annual statement. Also included in this section are schedules that reflect the growth of the company, NAIC Insurance Regulatory Information System (IRIS) ratio results for the period under examination, and the compulsory and security surplus calculation. Adjustments made as a result of the examination are noted at the end of this section in the area captioned "Reconciliation of Surplus per Examination."

Middlesex Insurance Company
Assets
As of December 31, 2003

	Assets	Nonadmitted Assets	Net Admitted Assets
Bonds	\$350,568,667	\$	\$350,568,667
Common stocks	18,037,236		18,037,236
Short-term investments	31,707,871		31,707,871
Receivable for securities	168,702		168,702
Investment income due and accrued	5,132,328		5,132,328
Premiums and considerations:			
Uncollected premiums and agents' balances in course of collection	6,058,669	547,822	5,510,847
Deferred premiums, agents' balances, and installments booked but deferred and not yet due	47,938,748	101,549	47,837,199
Accrued retrospective premiums	10,909,039	586,562	10,322,477
Reinsurance:			
Amounts recoverable from reinsurers	11,600,124		11,600,124
Funds held by or deposited with reinsured companies	424,214		424,214
Net deferred tax asset	19,245,518	5,665,791	13,579,727
Guaranty funds receivable or on deposit	58,960		58,960
Receivable from parent, subsidiaries, and affiliates	187		187
Write-ins for other than invested assets:			
Equities and deposits in pools and associations	24,510		24,510
Amounts receivable under high deductible policies	180		180
Total Assets	<u>\$501,874,953</u>	<u>\$6,901,724</u>	<u>\$494,973,229</u>

Middlesex Insurance Company
Liabilities, Surplus, and Other Funds
As of December 31, 2003

Losses		\$187,696,105
Reinsurance payable on paid loss and loss adjustment expenses		363,115
Loss adjustment expenses		37,286,171
Commissions payable, contingent commissions, and other similar charges		4,426,776
Other expenses (excluding taxes, licenses, and fees)		13,142,590
Taxes, licenses, and fees (excluding federal and foreign income taxes)		1,199,101
Current federal and foreign income taxes		2,507,917
Unearned premiums		78,667,985
Advance premium		478,930
Dividends declared and unpaid:		
Policyholders		580,910
Ceded reinsurance premiums payable (net of ceding commissions)		6,653,160
Funds held by company under reinsurance treaties		3,974
Amounts withheld or retained by company for account of others		159,276
Provision for reinsurance		452,035
Payable to parent, subsidiaries, and affiliates		2,928,351
Payable for securities		2,193,961
Write-ins for liabilities:		
Accounts payable—other		5,131,870
Premium deficiency liability assumed		200,000
Escheat funds		162,085
Reinsurance accounts payable—affiliates		443,293
New Jersey buyout expense		<u>387,500</u>
Total Liabilities		345,065,105
Common capital stock	\$ 4,200,000	
Gross paid in and contributed surplus	11,953,299	
Unassigned funds (surplus)	<u>133,754,825</u>	
Surplus as Regards Policyholders		<u>149,908,124</u>
Total Liabilities and Surplus		<u>\$494,973,229</u>

**Middlesex Insurance Company
Summary of Operations
For the Year 2003**

Underwriting Income

Premiums earned		\$160,702,792
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Deductions:

Losses incurred	\$107,111,391	
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Loss expenses incurred	16,620,818	
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Other underwriting expenses incurred	40,715,847	
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Write-ins for underwriting deductions:

New Jersey buyout expense	475,000	
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Total underwriting deductions		<u>164,923,056</u>
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Net underwriting gain or (loss)		(4,220,264)
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Investment Income

Net investment income earned	20,582,961	
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Net realized capital gains or (losses)	<u>(730,352)</u>	
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Net investment gain or (loss)		19,852,609
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Other Income

Net gain or (loss) from agents' or premium balances charged off	(843,011)	
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Finance and service charges not included in premiums	301,993	
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Write-ins for miscellaneous income:

Miscellaneous expenses	<u>(156,723)</u>	
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Total other income		<u>(697,741)</u>
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Net income (loss) before dividends to policyholders and before federal and foreign income taxes		14,934,604
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Dividends to policyholders		<u>1,063,402</u>
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Net income (loss) after dividends to policyholders but before federal and foreign income taxes		13,871,202
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Federal and foreign income taxes incurred		<u>2,054,000</u>
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Net Income		<u>\$ 11,817,202</u>
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Middlesex Insurance Company
Cash Flow
For the Year 2003

Premiums collected net of reinsurance		\$159,447,370
Net investment income		20,041,232
Miscellaneous income		<u>(697,741)</u>
Total		178,790,861
Benefit and loss related payments	\$91,470,113	
Commissions, expenses paid, and aggregate write-ins for deductions	53,638,956	
Dividends paid to policyholders	868,012	
Federal and foreign income taxes paid (recovered)	<u>825,588</u>	
Total deductions		<u>146,802,669</u>
Net cash from operations		31,988,192
Proceeds from investments sold, matured, or repaid:		
Bonds	\$58,534,560	
Miscellaneous proceeds	<u>2,193,961</u>	
Total investment proceeds		60,728,521
Cost of investments acquired (long-term only):		
Bonds	72,666,351	
Miscellaneous applications	<u>158,179</u>	
Total investments acquired		<u>72,824,530</u>
Net cash from investments		(12,096,009)
Cash from financing and miscellaneous sources:		
Other cash provided (applied)		<u>3,240,297</u>
Reconciliation		
Net change in cash and short-term investments		23,132,480
Cash and short-term investments, December 31, 2002		<u>8,575,390</u>
Cash and short-term investments, December 31, 2003		<u>\$ 31,707,870</u>

**Middlesex Insurance Company
Compulsory and Security Surplus Calculation
December 31, 2003**

Assets				\$494,973,228
Less security surplus of insurance subsidiaries				18,035,423
Add security surplus excess of insurance subsidiaries				15,235,423
Less liabilities				<u>345,065,105</u>
Adjusted surplus				147,108,123
Annual premium:				
Individual accident and health	\$	4,887		
Factor		<u>15%</u>		
Total			\$	733
Group accident and health		1,524,373		
Factor		<u>10%</u>		
Total				152,437
Lines other than accident and health		166,704,014		
Factor		<u>20%</u>		
Total				<u>33,340,802</u>
Compulsory surplus (subject to a minimum of \$2 million)				<u>33,493,972</u>
Compulsory surplus excess (or deficit)				<u>\$113,614,151</u>
Adjusted surplus (from above)				\$147,108,123
Security surplus: (140% of compulsory surplus, factor reduced 1% for each \$33 million in premium written in excess of \$10 million, with a minimum factor of 110%)				<u>45,551,801</u>
Security surplus excess (or deficit)				<u>\$101,556,322</u>

**Middlesex Insurance Company
Reconciliation and Analysis of Surplus
For the Four-Year Period Ending December 31, 2003**

The following schedule is a reconciliation of total surplus during the period under examination as reported by the company in its filed annual statements:

	2003	2002	2001	2000
Surplus, beginning of year	\$136,481,177	\$128,530,719	\$111,422,565	\$105,667,086
Net income	11,817,202	7,302,576	7,140,673	5,525,880
Net unrealized capital gains or (losses)	707,989	556,674	319,416	61,934
Change in net deferred income tax	(255,078)	(2,858,884)	7,826,862	
Change in nonadmitted assets	779,443	2,915,916	(8,333,823)	111,446
Change in provision for reinsurance	377,391	34,176	(464,691)	56,219
Cumulative effect of changes in accounting principles			10,619,717	
Surplus, end of year	<u>\$149,908,124</u>	<u>\$136,481,177</u>	<u>\$128,530,719</u>	<u>\$111,422,566</u>

**Middlesex Insurance Company
Insurance Regulatory Information System
For the Four-Year Period Ending December 31, 2003**

The company's NAIC Insurance Regulatory Information System (IRIS) results for the period under examination are summarized below. Unusual IRIS results are denoted with asterisks and discussed below the table.

	Ratio	2003	2002	2001	2000
#1	Gross Premium to Surplus	184%	180%	193%	187%
#2	Net Premium to Surplus	113	114	119	112
#3	Change in Net Writings	9	1	23	23
#4	Surplus Aid to Surplus	1	1	1	1
#5	Two-Year Overall Operating Ratio	90	92	93	92
#6	Investment Yield	5.5	5.8	6.0	6.2
#7	Change in Surplus	10	8	17	5
#8	Liabilities to Liquid Assets	77	77	80	78
#9	Agents' Balances to Surplus	4	5	6	6
#10	One-Year Reserve Development to Surplus	-6	-10	-16	-23
#11	Two-Year Reserve Development to Surplus	-11	-19	-30	-32
#12	Estimated Current Reserve Deficiency to Surplus	0	0	44*	29*

Ratio No. 12 measures estimated current reserve deficiency to surplus. The exceptional result in 2000 can be attributed to the change in the pool participation due to the acquisition of Select and Casualty from the John Deere Group. The exceptional result in 2001 is due to the 42% increase in unearned premiums.

Growth of Middlesex Insurance Company

Year	Admitted Assets	Liabilities	Surplus As Regards Policyholders	Net Income
2003	\$494,973,228	\$345,065,105	\$149,908,124	\$11,817,202
2002	444,443,471	307,962,299	136,481,173	7,302,576
2001	420,715,596	292,184,877	128,530,718	7,140,673
2000	377,454,467	266,031,903	111,422,564	5,525,880
1999	379,721,267	274,054,177	105,667,088	1,878,856

Year	Gross Premium Written	Net Premium Written	Premium Earned	Loss And LAE Ratio	Expense Ratio	Combined Ratio
2003	\$275,201,652	\$169,296,675	\$160,702,792	77.0%	24.7%	101.7%
2002	245,053,715	155,289,904	141,030,318	80.4	24.8	105.2
2001	247,573,064	153,522,133	135,937,045	81.9	24.6	106.5
2000	208,425,709	125,157,063	122,354,452	80.8	30.4	111.2
1999	238,116,481	102,084,522	82,801,446	76.6	30.0	106.6

The company grew steadily during the period under examination reporting a profit in each year with 2003 being particularly profitable. This is attributable to capital gains, due to good investment performance, and improved underwriting results in 2003. The company's expense ratio was relatively stable during the period under examination. Surplus, net income, net premium written and premium earned increased each year with 2003 being a particularly profitable year.

Reconciliation of Surplus per Examination

No adjustments were made to surplus as a result of the examination. The amount of surplus reported by the company as of December 31, 2003, is accepted.

VII. SUMMARY OF EXAMINATION RESULTS

Compliance with Prior Examination Report Recommendations

There were no specific comments or recommendations in the previous examination report.

Summary of Current Examination Results

Affiliated Companies

It was noted that the company did not include any amounts in Schedule Y, Part 2, Column 8. According to NAIC Annual Statement Instructions – Property and Casualty, Schedule Y, Part 2, Column 8, should include all revenues and expenditures under management agreements and service contracts, all income tax amounts resulting from intercompany tax-sharing arrangements, all amounts for contracts for services provided by the insurer or purchased by the insurer from other affiliates, and all compensation under agreements with affiliated brokers and reinsurance intermediaries; the introductory portion of these instructions prescribe materiality limits on what must be reported. The company's interpretation is that these limits apply and therefore the company left this schedule blank. Pursuant to s. Ins 40.04, Wis. Adm. Code, all affiliated, management and service agreements are material and therefore the amounts paid to or received from affiliates should be included in Column 8 of Schedule Y, Part 2, pursuant to s. 601.42 (3), Wis. Stat. It is recommended that the company properly complete Column 8 of Schedule Y, Part 2, in all future annual statements, by properly including all revenues and expenditures under management and service agreements pursuant to s. 601.42 (3), Wis. Stat., and s. Ins 40.04, Wis. Adm. Code.

Accrued Return Retrospective Premiums

During review of the accrued retrospective premium balance it was noted that the company is netting accrued retrospective premium receivables with accrued return retrospective premiums and reporting the netted balance on annual statement line 12.3. Statement of Statutory Accounting Principles (SSAP) No. 66, paragraph 6 a ii, states when an asset or liability is calculated for each risk, the total of all receivables shall be recorded as an asset and the total of all return premiums shall be recorded as a liability. SSAP No. 66, paragraph 8 a ii, further states that accrued return retrospective premiums shall be recorded as a write-in liability. It is recommended that the accrued return retrospective premiums be recorded in accordance with SSAP No. 66, paragraphs 6 a ii and 8 a ii.

VIII. CONCLUSION

Middlesex's operations are conducted under administrative agreements with its parent. Middlesex assumes 100% of the business written by Patriot General Insurance Company and has a 10% participation in the affiliated pooling agreement, whereby all property and casualty business written by the Sentry Insurance Group is combined and reapportioned. The experience of Middlesex's net premiums, liabilities, and net underwriting results follow the experience of the affiliated pool. The company grew steadily during the period under examination reporting a profit in each year with 2003 being particularly profitable. This is attributable to capital gains, due to good investment performance, and improved underwriting results in 2003. The company's expense ratio was relatively stable during the period under examination. Surplus, net income, net premium written and premium earned increased each year during the period under examination.

The examination verified the financial condition of the company as reported in its annual statement. There were no specific comments or recommendations in the previous examination report. No adjustments or reclassifications are being made as a result of this examination. Recommendations concerning properly completing Schedule Y, Part 2, of the Annual Statement and properly reporting accrued return retrospective premiums are being made as a result of this examination.

IX. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 34 - Affiliated Companies—It is recommended that the company properly complete Column 8 of Schedule Y, Part 2, in all future annual statements, by properly including all revenues and expenditures under management and service agreements pursuant to s. 601.42 (3), Wis. Stat., and s. Ins 40.04, Wis. Adm. Code.
2. Page 34 - Accrued Return Retrospective Premiums—It is recommended that the accrued return retrospective premiums be recorded in accordance with SSAP No. 66, paragraphs 6 a ii and 8 a ii.

X. ACKNOWLEDGMENT

The courtesy and cooperation extended during the course of the examination by the officers and employees of the company are acknowledged.

In addition to the undersigned, the following representatives of the Office of the Commissioner of Insurance, State of Wisconsin, participated in the examination:

Name	Title
Amy Wolff	Insurance Financial Examiner
Angelita Romaker	Insurance Financial Examiner
Eleanor Opprieht	Insurance Financial Examiner
Richard Anderson	Insurance Financial Examiner
Stephen Elmer	Insurance Financial Examiner
Randy Milquet	EDP Specialists
Tim VandeHey	EDP Specialists

Respectfully submitted,

Kerri L. Miller
Examiner-in-Charge